UNITED STATES TAX COURT
WASHINGTON, DC 20217

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Stephen E. McGrady & Patsy J. Powers, Stephen E. McGrady, Next Friend,	)	
Petitioner,	)	
v.	)	Docket No. 13015-07.
COMMISSIONER OF INTERNAL REVENUE,	)	
Respondent	)	

O R D E R

This case was on the Court's June 2, 2008 trial calendar for San Francisco, California. The Court took it off the trial track because the parties were working toward a settlement, but pretrial discovery led the Commissioner to move for summary judgment on all issues. McGrady, acting for himself and as his wife's next friend, answered the motion and it is now ready for decision.

The case is about the couple's 2002-04 taxes. The key issue is McGrady's deduction of an approximately $1.1 million loss in 2002 and 2003 (part of which carried over to 2004). McGrady asserts that he suffered this loss because a valuable proprietary database that he had developed became worthless in 2002 and 2003. He also contended in his petition that the Commissioner missed the statute of limitations for the 2003 tax year, and that the Commissioner was mistaken in determining that he owed the late-filing addition and accuracy-related penalty.

We address each issue separately, keeping in mind the usual admonition to draw all inferences in petitioners' favor and to always look out for genuine factual disputes.

The $1.1 million loss

The loss that is the only substantive issue in the case grew out of an idea McGrady had in the 1990s -- assembling an electronic database of the education, training, and experience of health-care professionals. McGrady and his wife thought that with this database they could make money from publications,

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software that would use the information to generate resumes, fees for job placement, and advertisements directed at those using the database. They created a business model that looked a lot like what became Monster.com and similar sites, but one that McGrady thought up at the dawn of the internet age, before anyone knew which such businesses would thrive.

McGrady and his wife incorporated MediMatch, Inc. as part of their plan. Doctors, nurses, and others in the field would submit their information for inclusion into the database on their own. Most of what they submitted was then posted on MediMatch's website. At its peak, in late 1999, the database held over a million records.

But, again according to McGrady's declaration, the website crashed as a result of a Y2K bug. MediMatch became a named party in the resulting class-action suit, but the database became increasingly stale, the lawsuit led to no substantial recovery, and McGrady eventually decided to take the position that the database had become worthless. He abandoned it, and took the loss on his tax return.

Supporting this loss proved problematic. The parties do not contend about whether the loss was an out-of-pocket cost to McGrady and his wife -- there is no genuine dispute that it was not. Instead, McGrady argues that he or MediMatch was the recipient of more than a million gifts -- i.e., the resumes -- from more than a million donors. By characterizing the submission of a resume to MediMatch as a donation, McGrady hopes to rely on IRC section 1015. That section establishes as a general rule that, in the case of donated property, the basis to the donee equals the lower of the basis to the donor or the fair-market value at the time of the donation.

McGrady submitted evidence on both types of valuation, and we assume in ruling on this motion that his valuations are true. Under the first method -- what he called the "cost-basis" approach -- his appraiser calculated a hypothetical, fully-allocated cost of creating a single resume (i.e., amortizing the cost of a home computer and software, and then adding an hourly charge for internet access and electricity); followed by multiplying the per-resume cost by the million or so resumes in the database at its height. (This is a bit of a simplification, but not much.)

Under the second method, his appraiser calculated the fair-market value of the individual resumes by examining sales of successful internet job databases, then dividing the sales price by the number of resumes in the databases. Multiplying the price per resume in these transactions by the number of resumes

in MediMatch's database yields what McGrady dubs the fair-market value of his database.

He now claims that the value of the database using a cost-basis approach was $3,014,635; and that its fair-market value was $3,855,000. Because section 1015 tells a taxpayer to take the lower number, he reported a basis of slightly more than $3 million. Since the database became worthless, he used the basis as the measure of his loss.

A threshold difficulty in analyzing the motion is that McGrady has taken different positions at different times in this litigation about whose loss this was. In a March 4, 2008 letter to the IRS, McGrady's lawyer referred to MediMatch as the owner of the database and owner of "the rights to in excess of one million resumes." In his papers answering the Commissioner's motion, however, McGrady takes the position that the donations were to himself, because the database belonged to him.

We look at both possibilities.

A. Donation to MediMatch. Though MediMatch is an S-corporation whose losses and income flow through to its owners, it is still a corporation. And that creates a problem for taking the loss because of restriction on basis calculations for property given to corporations. IRC section 362(c) trumps section 1015 and states that in the case of noncash property donated to a corporation from someone not a shareholder, the basis to the corporation in that property is zero. *See, e.g., Veterans Foundation v. Comm'r,* 317 F.2d 456, 458 (10th Cir. 1963). Since property with a zero basis cannot generate a loss deduction, see Treas. Reg. § 1.165-1(c); *Tonn v. Comm'r*, T.C. Memo. 2001-123, the Commissioner is entitled to summary judgment if the donations of the resumes were to MediMatch, rather than to McGrady directly. And that is true whether one uses the cost or market method -- section 362 tells us that the basis is zero either way.

So the key question for this part of the analysis is whether there is a genuine dispute as to whether the resumes were donated to MediMatch or to McGrady. We hold that there is no dispute because McGrady admitted in discovery that "for a person to make his resume information available to employers through MediMatch, a person must have submitted [a] resume or resume information to MediMatch." Ptrs. Resp. to Req. for Admis. No. 8. He has presented no evidence or explanation in his answering papers for why this isn't sufficient reason to disallow the loss -- there's no evidence from even a single submitter of even a single resume that he intended to donate it

at all, much less donate to either McGrady or MediMatch specifically.

A. Donation to McGrady. Nevertheless, caution compels us to examine the possibility of whether the result would change, were we to assume that the resumes were directly donated to McGrady.

1. The Cost Approach to Basis. We are dubious of the McGrady's purported "cost approach" analysis, which relies on the various expenses necessary for a job seeker to enter his resume information on Medimatch. IRC section 1012 says the basis in property shall be the cost of such property. A job seeker acquires his knowledge of his career history for no cost, making initial basis zero. However, he might incur some expenses to translate that knowledge into a Medimatch entry. IRC section 1016(a)(1) says the job seeker can then adjust his zero basis for "expenditures, receipts, losses, or other items, properly chargeable to capital account." But a Medimatch entry is, essentially, a resume, which is non-capital intellectual property like letters and memos. IRC § 1221(a)(3). Without a capital account, the taxpayer cannot adjust his basis, which remains zero.

McGrady's cost approach to calculating basis in property might indeed an acceptable one in some circumstances. But the Code limits the acceptability of this direct-cost-plus-allocation-of-indirect-cost approach to "real or tangible personal property produced by the taxpayer." IRC § 263A(b)(1). This section also says it "shall not apply to any property produced by the taxpayer for use by the taxpayer other than in a trade or business or an activity conducted for profit." IRC § 263A(c)(1). A job seeker who produces a resume is producing it for personal use not connected to a trade, business, or profit-seeking activity. It would not be appropriate for a job seeker to value his basis in his own resume using this type of valuation, making it similarly inappropriate for McGrady to claim this basis in each "gifted" resume.

2. The Fair-Market-Value Approach to Basis. That would leave McGrady with only the fair-market-value approach to rely on. But his answering papers calculate the value of the entire database in the market for databases. This is a misdirection play, because McGrady's argument -- that those submitting resumes to him or Medimatch were *donating* them -- means that we have to calculate the fair-market value of those resumes in the hands of those submitting them, not those receiving them for compilation in a database, because McGrady's theory is that basis flowed with the donation.

But can there be any genuine dispute as to what the fair-market value of these resumes were in the hands of those submitting them? More precisely, the question is what price would a jobseeking health professional pay for the nonexclusive right to use his own resume information. The answer has to be zero, because the professional retains broader rights -- the right to use that resume over and over again without restriction.

Our conclusion then, from all these perspectives, is that there is no genuine issue of disputed fact here; and that the Code requires us to rule in the Commissioner's favor on whether McGrady and his wife can claim the loss deduction.

That leaves several smaller questions, to which we now turn.

The Statute-of-Limitations Argument for 2003.

McGrady's petition alleged that the IRS issued a notice of deficiency for the 2003 too late to allow assessment. The Commissioner introduced a copy of the notice showing that it was dated March 7, 2007. McGrady's 2003 return was due on April 15, 2004. That leaves no genuine dispute that the Commissioner met the three-year deadline imposed by IRC section 6501.

The Accuracy-Related Penalty.

Because we agree with the Commissioner's disallowance of the McGradys' loss, arithmetic dictates that the McGradys substantially understated their tax liability. *See* IRC § 6662(d)(1)(A). McGrady's answering papers don't contest the penalty by raising the issue of whether he was acting reasonably and in good faith in taking this position. Positions not contested in opposing a summary-judgment motion are conceded. *Hughes v. Stottlemyre*, 454 F.3d 791, 800 (8th Cir. 2006); *Lanphere Enterprises, Inc. v. Jiffy Lube Int'l Inc.*, 138 Fed. Appx. 20, 23 (9th Cir. 2005).

And we also agree with the Commissioner that there is no genuine issue that McGrady -- who prepared his own returns for 2002 and 2003 -- was behaving unreasonably in trying to claim such a large loss on the abandonment of the database when he didn't pay for the resumes in the first place. Trying to avoid taxes by using fictitious losses to offset real income has to be supported by some reasonable argument or evidence to avoid summary judgment even on the accuracy-related penalty issue.

The Late-Filing Addition.

The Code imposes an addition to tax for failing to file a return on or before its due date. IRC § 6651(a)(1). The returns in the record are all dated after their due dates and were unquestionably received after their due dates. McGrady argues that these late-filed returns were only duplicates that he and his wife sent in after learning that the IRS had never received the originals. In his answering papers, he produced no copies of those earlier returns, and no certified-mail or overnight-delivery receipts, or any of the evidence that the Code requires to invoke the statutory-mailbox rule. (The general rule is that a return is filed when the IRS receives it, *United States v. Lombardo*, 241 U.S. 73, 76 (1916); there's an exception in the Code that treats a postmark as the equivalent of a receipt if the postmark is on or before the due date of the return. IRC § 7502. Elaborations of these rules are stated at great length in the Code and regulations -- together this body of law is the "statutory-mailbox rule.")

The problem for the Commissioner is that this case would be appealable to the Ninth Circuit. And the Ninth Circuit has long held that the statutory-mailbox rule did not eliminate the "common-law mailbox rule." *Anderson v. United States,* 966 F.2d 487 (9th Cir. 1992). The common-law mailbox rule treats timely mailing of a document as raising a rebuttable presumption that it was timely received by its addressee. *Id.* at 491.

Testimony alone is at least sometimes sufficient to meet the terms of this rule. *Id.* at 492. And in his answering papers, McGrady specifically swore that he timely mailed two of the three returns at issue -- those for 2002 and 2003. The Commissioner urges us to conclude that "petitioners' bare testimony will not be able to credibly contradict the information on the returns."

But whatever he thinks is the probability of his success at trial, the Commissioner must realize that summary-judgment motions are not the place for determinations of credibility. So we will not grant his motion as to the late-filing additions to the deficiencies for the 2002 and 2003 years. We will grant it as to the addition to the 2004 deficiency because McGrady failed to raise any issue of disputed fact on the addition for that year.

It is therefore

ORDERED that respondent's motion for summary judgment, filed September 10, 2008, is denied insofar as it seeks to determine an addition to tax under IRC section 6651(a)(1) for tax years 2002 and 2003. It is also

ORDERED that respondent's motion for summary judgment, filed September 10, 2008, is granted in all other respects. It is also

ORDERED that on or before August 19, 2009, the parties submit settlement documents or file status reports describing

(Signed) Mark V. Holmes
Judge

Dated: Washington, D.C.
June 19, 2009